



legal matters

Outlining a Buy-In From when to bring up the subject to how to get out if you need to, things you'll need to know to negotiate for your share of the practice.

BY JOHN ALLEVATO



Buying into a practice is as common today as ever. A physician who wants the most professional control and financial rewards from her medical practice will want to eventually become an owner. Yet, becoming an owner of an existing practice involves a number of complex issues, from the financial arrangements of the buy-in to what happens when the business relationship is terminated.

Too often, medical professionals buying into existing practices arrive unarmed, without professional help in

the negotiations. The physician buying into the practice may have been practicing there for a number of years, and feels that he can trust the owner or owners of the practice. Other times, the purchasing physician feels it may be unseemly to engage professionals to assist him in this process, perhaps afraid this will offend the current owners. Or maybe the purchasing physician isn't aware that a professional could be of service.

It's too important a matter to take any chances. The buy-in will be one of the most significant financial decisions you make during your lifetime. In addition, there is a 'marriage-like' quality to entering into a business partnership with another medical professional or group of professionals. You must consider how to enter the negotiations, what should be included in the negotiations, and how to resolve some of the more significant

issues which may arise.

Broaching the subject

I am frequently asked when the matter of becoming a partner, or buying in, should be brought up by the physician or the group. Invariably, my answer is 'as soon as possible.' The answer is the same whether I am speaking to the medical group or to the physician buying into the practice.

While this subject may not be the most important part of the negotiations surrounding joining a practice, it should be higher on the list than it is usually. It may be awkward to start negotiating a buy-in package when you first join a group for any number of reasons, but that doesn't preclude getting some-

Finding out when you would first be considered for ownership, or at least discovering how one who is asked to buy in does so and how much it costs are appropriate points of discussion from the very beginning.

LEGAL MATTERS

Continued from previous page

thing in the employment agreement stating when these discussions will first take place. Your initial agreement also should indicate when you would first be considered to become a partner of the group and under what terms and conditions.

For example, let's assume you are a physician getting ready to leave a fellowship or residency program and have interviewed with a medical group in the geographical location you wish to settle. There is mutual interest in your joining the group, so they make an offer which you accept. A week later they send you an employment agreement. Nowhere in the agreement does it speak of when, or if, or how, you would become an owner of the group.

Do you bring up the issue?

The answer, of course, is yes, bring it up. How to do it is more problematic. It may be uncomfortable, but asking about the process is in order. Finding out when you would first be considered for ownership, or at least discovering how one who is asked to buy in does so and how much it costs are appropriate points of discussion from the very beginning. Don't expect a commitment from the group—remember, they probably have not seen your work or your interaction with patients. But asking about their expectations of your performance and productivity is a legitimate inquiry.

Try to get some guidance into the employment agreement. While the group probably will not guarantee that you'll become a partner, some assurance that you would be considered in a couple of years or so is not an unreasonable request. Along those lines, also ask for a formalized review every so often (semi-annually perhaps), so you can gauge how you are doing and if you are meeting the group's expectations. A smaller group may do this informally; if so, then seek it out. For larger groups with professional

managers and multiple offices, try to get a commitment in the employment agreement to at least have the semi-annual review, and learn at that time whether you are progressing on track. It is best to get in writing when you would first be considered to buy in, and under what terms and conditions.

The circumstances under which the buy-in will be considered also should be established at the inception of the relationship between the parties to avoid conflict later. Consideration for buy-in can occur after the passage of a certain amount of time, or after a significant event, or upon reaching production milestones. In any event, make sure the triggering mechanisms are clear from the beginning.

Typical mechanisms

The ways in which physicians buy into existing practices are as varied as the practices themselves. I have seen no one formula or method for how this is done. However, there are some similarities in the methodology.

First, the method should allow the physician to calculate a cost of the buy in. For example, if a formula is used, the physician, in consultation with his advisers, should be able to calculate a price. Sometimes financial information about the group is necessary which may or may not be readily available. If the formula utilizes fair market values of assets, appraisals of those assets may have to be conducted to determine the buy-in price.

Just as how the price is determined varies, so does the method by which the buy-in price is computed. From a broad overview, the purchase price may include purchasing a share of the tangible assets of the practice, plus some amount for the receivables in place. It is also common for this to be determined by the revenues of the group; how much money does the

practice generate, for example? The price may then be calculated as a percentage of annual revenues, or revenues generated by the purchasing physician. A professional who is experienced in these matters can help.

Second, the method of payment of the purchase price should be established. Often this portion of the contract is the most important as many physicians new to the practice have not had the opportunity to accumulate much wealth, and most are paying off medical school debts. Sometimes the medical group will finance the buy-in—by that, I mean the practice provides payment terms, thereby sparing the physician the need to borrow from a bank or other source. This convenience might also translate into terms which are more tax-favorable for the purchasing physician, perhaps by allowing him to take a pay reduction, thereby paying with pre-tax dollars. Those are details which must be worked out with the assistance of a tax professional. This form of assistance is not always available; the medical group may not want to act as a 'bank' and may just want the buy-in payment from whatever source the purchasing physician can tap.

The method of buy-in agreed upon by the parties will have tax consequences to both sides. The purchasing physician would like to buy in with dollars that are not first subject to tax, as mentioned above. The medical group would like for the buy-in to generate payments which are taxed at a lower capital gains rate rather than at ordinary income rates. For example, existing shareholders can sell stock to the physician buying in rather than shifting around pre-tax dollars. The dollars don't go to the medical corporation in this case, they are paid to the other physicians. Most often these goals are in direct conflict with each other. One side usually does not get what it wants,

LEGAL MATTERS

Continued from previous page

so a compromise has to be reached.

Terminating the relationship

Once you're entering a buy-in agreement, there are a whole new set of issues to hash out. One important one is how either party might get out of the agreement. Not surprisingly, many disputes arise when a physician leaves. In order to protect your investment in the group, it is important to articulate as specifically as possible the events that might cause you to be terminated. Whether that termination is voluntary or involuntary, it is critical to set out in the agreement the financial terms of the disentanglement.

For example, do you get your buy-in amount back? Do you get an amount which includes the value of the receivables which your work generated but which haven't yet been collected? How is the buy-out amount to be paid? Would it be distributed as a lump sum or over time, say, as the receivables are collected? Under what circumstances are the provisions of a non-compete covenant applicable, and for how long?

Negotiating all these matters specifically at the outset can help avoid many potential disputes down the road. Both sides should take care to include these provisions in a physician's employment agreement to ensure that the relationship is mutually rewarding and that both the physician and the group understand the other's expectations from the beginning. ■

John Allevato is a member in the Charleston, West Virginia, law firm of Spilman Thomas & Battle, PLLC, where he practices business and tax law. He routinely advises and counsels health-care entities and physicians. He is a member of American Health Lawyers Association and can be reached via e-mail at jallevato@spilmanlaw.com.